Comment on Recent Cases

BILLS AND NOTES: NON-NEGOTIABLE PAPER: SUCCESSIVE ASSIGNEES—The evolution in jurisprudence of the idea of negotiability and its extension to certain classes of technically non-negotiable business instruments goes steadily on. In *Security Mortgage Company v. Delfs*[1] the payee of a mortgage and note delivered them to a bank and executed a separate assignment; the bank voluntarily redelivered to its assignor (who gave a receipt therefor) the said note and mortgage while still unrecorded without notation thereon of the transfer; the payee proceeded to sell the redelivered instruments to a bona fide second assignee; six months after the first transaction and one month after the second, the bank recorded the assignment; four days later the second assignee recorded; in the foreclosure suit the second assignee prevailed.

The effect of the recording acts was eliminated by reason of a supreme court holding[2] that section 2934 of the Civil Code, under which the recording of an assignment of a mortgage is notice only to those subsequently deriving title from the assignor, controls section 1107 which favors the bona fide grantee who records first. The simple question thus was presented: Does the second assignee of a non-negotiable instrument prevail over the first if the assignor had lawful possession of the paper at the time of the second sale?

Ordinarily, if neither assignee of a chose in action gives notice to the debtor, the first in time prevails. Alongside this conception of static[3] security embodied in the maxim *nemo dat quod non habet* and in the general rule of law that a person cannot legally be deprived of his property by the act of a third person, there is another conception, its necessary counterpart, which Demogue has termed "dynamic."[4]

"The owner of a right loses all or part of the advantages which it bestows when this result seems useful in the interest of a third person who can reasonably have believed that such a right did not exist."[5] The outstanding example of dynamic security is

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[1] (May 20, 1920) 32 Cal. App. Dec. 322.

[2] Adler v. Sargent (1895) 109 Cal. 42, 49, 41 Pac. 799, Ann. Cas. 1918C 486, note.

[3] See Modern French Legal Philosophy, Chapter XIII, "Security," by René Demogue, vol. VII of The Modern Legal Philosophy series (1916) p. 428 ff.

[4] Idem.

[5] Idem, p. 427.

that of the rights acquired by the holder in due course of negotiable paper. It is an ancient and familiar rule that a bona fide transferee of a negotiable instrument gets good title even from a thief.[6] Possession of the document, lawful or unlawful, in empowering the possessor to transfer the bundle of rights, powers, privileges and immunities collectively labelled "title," is the keystone of the legal structure of negotiability.[7]

The struggle between the concepts of dynamic and static security, Demogue contends, is more inextricable than it seems, for the owner of today is the acquirer of yesterday. "If . . . . the Civil Code favors me when I acquire an instrument to bearer, it becomes a menace when I confide that instrument to a banker or depositary, who may sell it."[8]

The decisions apparently reflect the struggle. The mercantile need for facilitating trade and rendering commercial transactions certain and secure gave rise to the principles of the law merchant and the whole theory of negotiability which favors the third person even though he secured the paper from a thief.[9] Although that same business need is constantly in evidence in the case of certain classes of technically non-negotiable commercial paper which circulate freely in the open market (stock certificates, bonds, and in the instant case, a promissory note secured by mortgage), the law has not gone to the extreme length of disentitling the owner where possession was taken from him through theft.[10] But if he voluntarily entrusts a stock certificate with an assignment in blank and a power of attorney to one who later wrongfully disposes of it to an innocent purchaser,[11] or if the assignee for security of an ordinary contract even after notice to the debtor permits the assignor to retain possession of the paper,[12] or if he redelivers a note and mortgage to the payee thereof who then assigns a second time,[13] the law will protect the bona fide buyer. In these circumstances the person in lawful possession of these non-negotiable choses in action seemingly is invested with a power of transferring

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[6] See illuminating opinion of Hon. David Leventritt in the case of Brown v. Perera (1918) 176 N. Y. Supp. 215, affirmed by the Appellate Division, 182 App. Div. 922, 169 N. Y. Supp. 1086.

[7] For an excellent treatise of this proposition see article by Professor Zechariah Chafee, Jr., in 31 Harvard Law Review, 1104, 1112 ff.

[8] Supra, n. 3, p. 430.

[9] Supra, n. 6. See 33 Harvard Law Review, 263, for comment on Pratt v. Higginson (1918) 230 Mass. 256, 119 N. E. 661, where brokers who sold stolen bonds and paid the proceeds to the thief were held not liable to the former owner for conversion.

[10] Chase v. Whitmore (1886) 68 Cal. 545, 9 Pac. 942; Kohn v. Sacramento Electric Gas etc. Co. (1914) 168 Cal. 1, 141 Pac. 626, 2 California Law Review, 377, 392, 393; Crocker National Bank v. Byrne & McDonnell (1918) 178 Cal. 329, 173 Pac. 752.

[11] Fowles v. National Bank of California (1914) 167 Cal. 653, 140 Pac. 271.

[12] Phelps v. Linnan (1916) 174 Iowa 138, 156 N. W. 294.

[13] Supra, n. 1.

the true owner's title to a third person. The phenomenon is another example of dynamic security.

While the language of the courts appears to emphasize so-called equitable maxims,[14] is it not rather the judicial tendency towards effecting negotiability of certain choses in action freely and continuously exchanged in the business world that lies fundamentally at the base of the decisions? It is a long judicial evolution from the early common law rule that choses in action were not assignable at all[15] to the proposition that the principal case would tend to establish, that they may be assigned by the one in lawful possession. Will the next step in this development be the preference of the innocent third person even though the seller unlawfully secured possession?[16] *J. J. P.*

CONSTITUTIONAL LAW: FOURTEENTH AMENDMENT: TAXATION FOR PUBLIC PURPOSE: NORTH DAKOTA INDUSTRIAL PROGRAM—From within the quiet sanctum of the Federal Supreme Court on June 1, 1920, in the form of a decision written by Justice Day, upholding the constitutionality of North Dakota's statutory industrial progam, reverberated the judicial echoes of the political and economic battle now being waged in that commonwealth.[1] Validity of legislative acts under which the state of North Dakota is to engage in the businesses of banking, manufacturing and marketing of farm products and operating a warehouse, elevator and flour mill system, and building of homes for its residents, was sustained in *Green v. Frazier*[2] against the contention that taxes to be raised for the enumerated purposes were for a private use and amounted to a deprivation of plaintiffs' property without due process of law. In affirming the decision of the Supreme Court of North Dakota in *Green v. Frazier*,[3] Justice Day reiterated the long-established attitude of the court that the judgment of the highest tribunal of the state declaring a given use to be public in its nature would be accepted unless clearly unfounded. It is significant that no case is recalled where the Supreme Court has condemned as violating

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[14] "Where one of two innocent persons must suffer by the act of a third, he, by whose negligence it happened, must be the sufferer." Supra, n. 1, p. 324.

[15] 5 C. J. 846. The pendulum of assignability seems now to have swung to the other extreme so that it is not illogical to apply the rule against restraints of alienation of chattels to a debt, according to a dictum by Justice Holmes in Portuguese-American Bank v. Welles (1916) 242 U. S. 7, 11, 61 L. Ed. 116, 37 Sup. Ct. Rep. 3.

[16] For the history of the treatment of choses in action by the common law see article by W. S. Holdsworth, 33 Harvard Law Review, (June, 1920) 997-1030.

[1] See World's Work, October, 1916, pp. 678-689; Review of Reviews, April, 1918, pp. 397-400; Survey, March 1, 1919, pp. 753-760; Atlantic Monthly, May, 1919, pp. 686-696.

[2] (June 1, 1920) 40 Sup. Ct. Rep. 499, U. S. Adv. Ops. (1919-20) 625.

[3] (January 2, 1920) 176 N. W. 11.